



Directors

William B. Boggs
President & Chief Executive Officer

Norman J. Brown
Chairman of the Board of Directors

Robert E. Heneault
Vice-President Administration
The Steel Company of Canada Limited

Douglas S. Lyall
Vice-President Finance
Gulf Oil Canada Limited

S. Keith McWalter
Vice-President Planning & Control
Gulf Oil Canada Limited

Morgan C. Payne
Senior Vice-President Finance & Administration
The T. Eaton Company Limited

William C. Rankin
Special Assistant to the President
The T. Eaton Company Limited

Corporate Headquarters

2599 Speakman Drive
Mississauga, Ontario L5K 1B1
(416) 822-5200

Auditors

Thorne Riddell & Co.

Branch Offices

The Metropolitan Life Building
99 Bank Street
Ottawa, Ontario K1P 5K4
(613) 233-5673

205-5th Avenue S.W.
Bow Valley Square 2
Calgary, Alberta T2P 2N4
(403) 263-8010

12 Sheppard Street
Toronto, Ontario M5H 3A1
(416) 864-1328

Officers

Norman J. Brown
Chairman of the Board of Directors

William B. Boggs
President & Chief Executive Officer

John C. Bright
Vice-President Data Processing Services

David Herd
Vice-President Finance & Administration
Secretary-Treasurer

Herbert E. Hilgenberg
Controller & Assistant Secretary

Harry G. Porteous
Vice-President Marketing

Solicitors

McCarthy & McCarthy

Bankers

The Bank of Montreal
The Toronto-Dominion Bank

Subsidiaries

Digital Methods Limited
1736 Courtwood Crescent
Ottawa, Ontario K2C 2B5
(613) 225-1171

L & W Data Systems Limited
12 Sheppard Street
Toronto, Ontario M5H 3A1
(416) 864-1676

MAR 28 1979

2599 Speakman Drive
Mississauga, Ontario L5K 1B1
Telephone (416) 822-5200

W.B. Boggs
President

April 28, 1978.

Mr. Timothy Pritchard,
Globe & Mail,
444 Front St. W.,
Toronto, Ontario,
M5V 2S9.

Dear Mr. Pritchard:

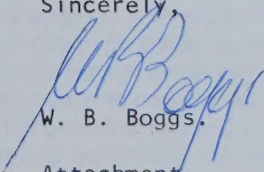
Attached is a copy of our Annual Report which I felt would be of interest to you. This is our first published Annual Report since we opened for business in December 1971.

Canada Systems Group is privately owned, and although there is no requirement for such public disclosure we feel a responsibility to advise our rapidly growing customer base and others on the progress of the Company.

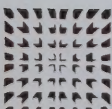
1977 was a very satisfactory year for Canada Systems Group, with record pre-tax earnings of \$1,765,000, and an increase in net earnings after extraordinary items of 63% over 1976. Cash flow increased 58% and total revenues increased by 11% to nearly 27 million dollars - a significantly larger revenue than any other Computer Services company in Canada.

We look to 1978 with confidence and to the future with enthusiasm.

Sincerely,


W. B. Boggs.

Attachment





President's message

This is the first Report to the Shareholders to be published by our Company, which was incorporated in April 1971. Although the Company is privately owned, and there is no requirement for such public disclosure, we feel a responsibility, as a supplier to our rapidly growing customer base, to advise them of the progress of our Company.

We commenced operations in November 1971 in our custom-designed facility located in Sheridan Park, Mississauga. Since that time, the Company has grown steadily to a revenue base of approximately \$27,000,000 in 1977, and is now the largest Computer Services company in Canada (excluding IBM).

The objectives of our Company as originally stated were "to provide a broad range of computer-based information system services to Industry and Government". These objectives have been consistently kept in the forefront, have stood the test of time, and have led us to provide the broadest possible range of computer-based services — from application packages to the replacement of inhouse hardware.

Despite the economic difficulties that have plagued the Canadian business scene during 1977, the business picture for Canada Systems Group has been a good one. Our sales revenue was up by 11% over 1976 — an enhanced product line, coupled with greater market penetration, are the major reasons for continued growth and the addition of major accounts in both the public and private sectors. Our profit performance and cash generation are on target.

Because of changes in technology, our industry has severe limitations upon its ability to adjust prices to offset increased costs. To remain profitable it is necessary to continually offer improved services and to devise new means of operating more effectively by taking advantage of rapidly improving technology. We incorporate new developments as quickly as possible, but we make changes cautiously to ensure that the quality of service to our many customers is not affected.

Competition in 1977 has increased through aggressive pricing from relatively new entrants to the industry, the reduction in costs of large scale computers, and the impact of more powerful mini-computers. However, because of our demonstrated ability to utilize mini-computer technology as appropriate and to incorporate new technology as quickly as is practical, while maintaining the highest quality of service at a fair price,

we believe we are well positioned to withstand competition and to continue to grow. Our customer loyalty is one of our greatest strengths.

The support of management and employees during 1977 has been excellent. Through tight control and enthusiastic participation by managers, our overall productivity continued to increase, as evidenced by the continued growth in Sales per Employee.

Our computer subsidiary DML, located in Ottawa, had a reasonably successful year. Government spending in the areas of this company's mini-computer based expertise increased, and their continued investment in new commercial products is beginning to show positive results.

L & W, our Toronto based mini-computer turnkey subsidiary, had a difficult year. A major reorganization was undertaken and the impact has been fully absorbed in this year. We are reasonably confident that the problems are behind us and that future growth will support our entry into this market.

I believe that the Computer Services Industry has achieved a considerable degree of maturity in 1977, and will continue to grow in a dynamic and viable manner. We offer a valuable service to Canadian business by making the most modern and sophisticated data processing equipment and services available to companies of all sizes at costs well below those which they individually could realize. Our services provide many companies with the opportunity to conserve their resources, to modernize and expand their operations and research in a very cost effective manner, allowing them to compete effectively with larger companies in Canada and abroad.

We look to 1978 with confidence. We are planning major investments in new technology both for hardware and software, as well as continued investment in new products and in the use of distributed processing techniques. We are supported by a well trained and competent staff who are motivated to provide top quality service. Technology will continue to change rapidly, but we are convinced that we are well positioned to capitalize on our investment in this exciting, rapidly growing and changing business. With our capacity to adapt to change, our innovative approach and the confidence placed in us by our customers, we look forward to the future with enthusiasm.

President and Chief Executive Officer

Company history

Canada Systems Group was established in 1971 by Eaton's, Stelco and TRW Inc. to provide computer-based information systems services to industry and Government, using two IBM 370, Model 155 computers. The computers were installed in a unique building of 130,000 square feet, specifically constructed as a datacentre and located in Sheridan Research Park, Mississauga. A group of highly qualified systems, programming, and technical personnel was recruited to support our concept of providing a complete service to our customers. From this initial base, we now provide on state-of-the-art computers a wide range of data processing services to hundreds of customers, both large and small.

In 1972, the Company's first full year of operation, sales were \$6 million and the Company operated at a loss. During this period, the management and staff were primarily engaged in launching the Company, satisfying the owners' needs, and developing an organization capable of supporting the Company's objectives. Therefore, little impact was made in the outside market.

In 1973, sales were \$9 million, reflecting an aggressive approach to the market and a growth rate of 50%. CSG in the same year acquired control of Digital Methods Limited, an Ottawa based company providing specialized scientific and commercial consulting and installation services. The Company was still unprofitable but to a lesser extent than in 1972. The TRW equity holding in CSG was purchased by Eaton's and Stelco during the year. Major changes in CSG computing environment were made in 1973 when CSG installed the first IBM 370, Model 158 computer in Canada and later in the year installed an IBM 370/168 computer, replacing the original computer equipment.

In 1974, sales grew to \$14 million, reflecting a 56% growth rate. In the same year, Gulf Canada joined CSG first as a customer, and then as a full equity partner. In 1974 CSG came close to breaking even for the year.

In 1975, sales were \$20 million and L & W Data Systems, a Toronto based company that has been engaged for over ten years in the development and installation of mini-computer based business systems, became a wholly-owned subsidiary. This represented a further commitment to provide a fully integrated range of services. By mid-year, CSG had achieved profitability on a monthly basis, but ended the year with a small deficit due to unprofitable operating results in the first six months. Early in 1975 a second IBM 370, Model 168 computer was installed replacing the IBM 370/158.

In 1976, the patient investment in both people and capital yielded a consolidated profit in excess of \$700,000, with total revenue increasing to almost \$24 million, an 18% increase over 1975. Revenue from data processing increased by 35%, and by the end of 1976, revenue from the two original owners of CSG represented less than 38% of total revenue, compared to almost 100% in 1972. More technical changes and innovation than in any previous year were made in 1976. These included the successful installation of the first IBM Attached Processing Unit in Canada, which resulted in a 35% increase in our computer capacity, and the implementation of the latest IBM software operating systems to ensure that we maintained our technical leadership. Completion of our National Communication Network which provides direct entry capability to our central site computers from twenty major cities across Canada, made us a truly national organization, supported by a rapidly emerging branch network.



EXECUTIVE COMMITTEE: left to right — Brian W. Marshall, Manager Personnel; John C. Bright, Vice-President Data Processing Services; William B. Boggs, President and Chief Executive Officer; David Herd, Vice-President Finance and Administration; Harry G. Porteous, Vice-President Marketing.

In 1977, total revenue for CSG, excluding subsidiaries, increased to \$22,562,000 a 13% increase over 1976. Data processing revenue increased by 20%; however, revenue from the labour intensive areas such as customized program development and consulting services declined by 21%. This decline was due in large part to the elimination of certain activities which were outside the main business thrusts of CSG and concentration of some human resources on the implementation of packaged application software.

The success of data processing selling resulted from a broad spectrum of business situations and the addition of some forty new customers during 1977. For the second consecutive year, prices were not raised.

For several years, CSG has been providing application software packages for the use of its customers. These take the form of functional packages such as general ledger, accounts payable and accounts receivable for a broad range of customers, and industry-oriented products such as our credit union system. During 1977, significant additions and upgrades were made to these software offerings. In the general accounting field, a new payroll system was installed and interfaced to the general ledger system. A materials inventory system was marketed for the first time. Several additions were made to the suite of analytical and econometric packages offered by CSG. One of these is SIMPLAN, a multi-purpose planning, budgeting, and modelling system which provides many advanced and unique features. It can be easily mastered and used as a decision-making tool by non-technical managers, planners and financial analysts with no previous experience in computer modelling.

In the area of industry-oriented application products, the most significant advance was the announcement of CONTACT (CSG's On-Line Teller and Administrative Control Terminal System) designed for use by the financial community. Intended to replace the batch banking service which CSG has provided for the last five years, CONTACT has been extremely well received and the first users will be going on-line in early 1978.

The service offerings of CSG also were enhanced during 1977. A sharable data-base product, System 2000,

was introduced early in the year. The APL programming language which can be easily accessed interactively using TSO was made available. Another significant announcement was the introduction of a greatly improved demand processing environment for all customer-controlled jobs. The highlights were the establishment of three categories of jobs: non set-up, regular and special production jobs. For each of these job categories, target times have been published together with an expansion of CSG's service guarantee on turnaround times which will help to provide the necessary flexibility for superior service on a sustained basis. This new environment will be effective in April of 1978.

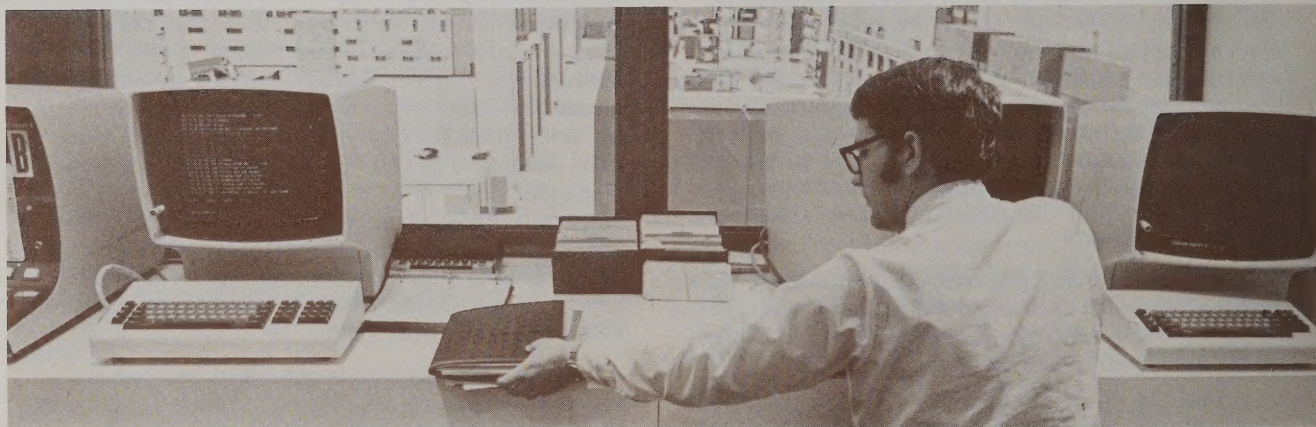
It has been CSG's plan to expand its geographic coverage through the appointment of agents in principal cities across Canada. These agents are local independent datacentres who offer CSG products and services to their customers and prospects in their specific areas. During 1977, four new agents were appointed extending CSG's nationwide service to a total of eleven cities.

In June, CSG's Ottawa branch office moved into new, expanded quarters in that city's core. At the same time, the size of the staff was doubled. Both of these events reflect CSG's rapidly growing penetration of the Canadian Federal Government market.

In October, a downtown Toronto branch office was opened to provide complete over-the-counter and interactive processing facilities for our customers in that area. Our Calgary office also moved into larger quarters at the beginning of 1978. With these new facilities, Canada Systems Group can now offer a much broader range of services to our customers in these three cities.

All of the the above improvements in products, services and geographic coverage greatly assisted in producing the significant revenue gains of 1977 and have positioned CSG for entry into 1978 with high expectations for continued growth.

Operations review



The Canada Systems Group was founded, and has always operated, on the basis of an uncompromising commitment to quality of service. Such a commitment can be met only by providing high calibre people with state-of-the-art tools and techniques and we are very proud of our accomplishments in both regards.

Our specially designed building houses two of the largest computers currently available surrounded by a vast array of peripheral and communications equipment and staffed around the clock by highly trained operating crews. A comprehensive back up strategy, ranging from fully backed up Hydro sources to shared files and libraries, provide our customers with the most reliable service available in the industry.

During 1977, our service was further enhanced by the provision of a full MVS Operating Environment, conversion of most of our disk pool to the state-of-the-art 3350 technology, and the initial step towards upgrading our magnetic tape pool to the high density, high speed 6250 bit per inch technology. These and other changes were part of our continuing commitment to provide the most cost effective and most reliable service possible.

The Canada Systems Group was the first data services company in Canada to establish a teleprocessing control centre. The centre was initially created in 1975 and has since been widely emulated. It is staffed at all times and is responsible for managing our coast-to-coast communications networks and for constantly monitoring the service as seen by our remote access users at their end. This monitoring is done by specially trained staff

aided by a variety of hardware tools some of which were designed by CSG personnel and custom built to their specifications.

CSG's networking capability was enhanced during 1977 by the addition of intelligent network processors in both Mississauga and Calgary. These new processors employ a technique known as statistical multiplexing to dramatically improve the throughput of conventional lines yielding improved service to our customers.

Several major new applications were added to both our private and shared networks during 1977 and the T.P. Control Centre now manages a wide range of critical on-



line systems running almost 24 hours a day and servicing approximately 600 terminals in customer sites from the Maritimes to Vancouver. They are, and will continue to be, supported by the best people and facilities available anywhere.

Physical and data security are of utmost importance to all our customers and we believe our facilities more than adequately deal with both dimensions.

Physical security is inherent in the special design of the building itself and supplemented by such things as TV monitoring systems, smoke and fire detection systems, controlled access doors, uninterruptable power supply, bank type vaults, and shared multiple processors.

Data security includes both inter and intra user methods designed to prevent unauthorized access to data by both customer personnel and others. These facilities are constantly maintained and updated to ensure the highest possible levels of security and integrity.



Like any successful enterprise, our success depends on people and we are extremely proud of ours. The Data Processing Services Division staff includes a large number of computer professionals available as consultants to our customers in a wide variety of areas including data base, systems design, systems optimization, networking, and programming.

All of our internal technical projects are planned and managed by senior technical consultants all of whom have many years experience in the extremely complex environment of a large, multi-CPU installation. They are responsible for the evaluation, selection, and implementation of all operating system software and utilities that are so very vital to the efficiency and stability of our service. The principal technical emphasis during 1977 was directed toward the installation of the MVS Installation Productivity Option (IPO) during the second quarter and Multi Access Spool, which will be available early in 1978. A great deal of activity is currently underway in the areas of advanced communications function and data base systems. As always, our greatest assurance of success is the knowledge that the activity will be in the hands of the best people in the business.



Financial highlights

The financial year ended December 31, 1977 was a most satisfactory year for CSG, one in which our financial condition continued to improve. Financial results were the best ever achieved with consolidated net earnings after extraordinary items, increasing by 63% over 1976 to \$1,150,912. More importantly, the cash flow increased by 58% to a record of \$3,265,052 and total consolidated revenues increased by 11% to \$26,425,733.

In 1977, the Balance Sheet for the Company was strengthened to a far greater extent than is reflected by the earnings reported for the year. The earnings as reported are net of the write-off of Goodwill in the amount of \$562,811 and a write-down of inventory of \$217,000. These items reduced consolidated earnings from the \$1,900,000 range to \$1,150,912 as reported on the Income Statement. The net result of these actions is an improvement in our equity base combined with significant enhancement in the quality of the assets of the Company.

When L & W was acquired, a substantial base of intangible assets existed in the form of established technical and application knowledge. However, rapid changes in technology and changes in customer requirements reduced the value of these intangible assets, therefore, we decided to write-off the Goodwill in L & W in 1977. Recent commitments to L & W make us optimistic about the future of L & W and the market it serves.

Total consolidated revenue increased by 11% over 1976, with Data Processing revenue from customers of CSG only, excluding owner-generated revenue, increasing by 57%. This emphasizes the continued confidence and satisfaction of our existing customers and our ability to attract new customers to the CSG environment.

The increased sales in 1977 were achieved without resorting to any increase in our prices. Despite this action and the significant cost increases absorbed in 1977, the sales levels achieved enabled CSG to significantly increase its profit margins in the year.

In 1977, we continued to invest in new technology and to increase our capacity as necessary to continue to provide a high level of service to our customers, with Capital Expenditures of over \$3,000,000. A significant portion of this is shown on our Balance Sheet by the

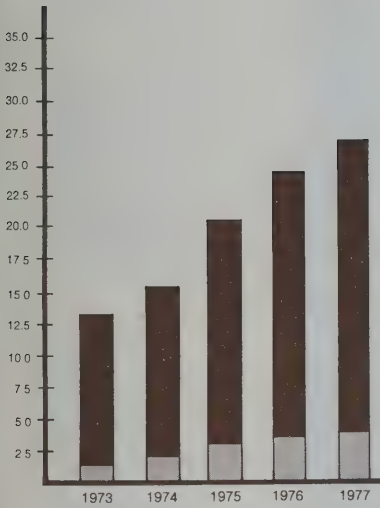
increase in long term loans, reflecting a policy of purchasing equipment rather than leasing, as was our original strategy. This policy is made possible by our very positive cash flow which was larger than our new commitments in 1977 and our projected commitments for 1978. Continued positive cash flow combined with the established support of our bankers will be sufficient for CSG to realize all of its planned objectives and to achieve its long term plans. This financial strength is particularly important in an industry where capital requirements are large and change occurs rapidly.

The 1977 achievements can be appreciated when looking at a few standard financial ratios. The current ratio improved from .74/1 in 1976 to .92/1 in 1977. The Return on Investment in 1977 was 21.9% compared to 13.4% in 1976 and the Return on Capital employed in 1977 was 7.1% up from 4.8% in 1976. If the extraordinary write-off of the Goodwill in L & W were excluded, the Return on Investment and the Return on Capital Employed in 1977 would be 32.6% and 10.6% respectively. These results indicate that the commitment of our owners to sacrifice early financial return for quality and excellence has built the solid foundation which made the improved financial results possible in 1977.

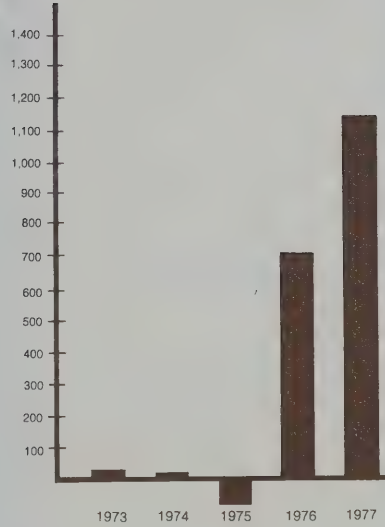
In our early years, profits were elusive due to the cost pressures associated with launching a new Company and implementing our commitment to excellence and pursuing our objective of becoming the industry leader. However, in the past two years and particularly in 1977 these strategies have shown encouraging results as evidenced by our rising sales per employee.

Achieving the 1977 profits while maintaining our 1975 prices and absorbing significant cost increases in many areas reflects favourably on the dedicated efforts of our management team. Despite significant cost increases anticipated in most areas for 1978, we again plan to maintain our existing prices. This policy is made possible by the continued improvement in our productivity and the support from an ever increasing group of customers who appreciate our efficient and cost-effective operation.

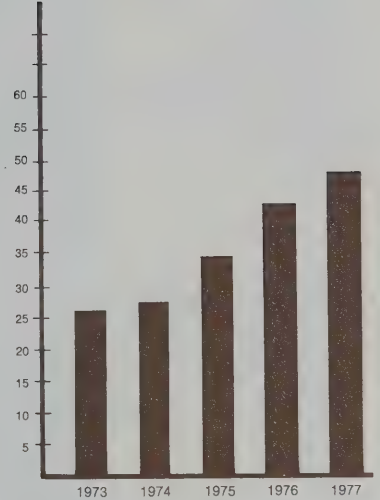
SALES
(\$ millions)



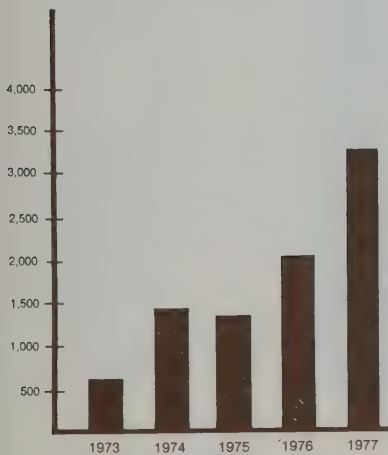
EARNINGS
(\$ thousands)



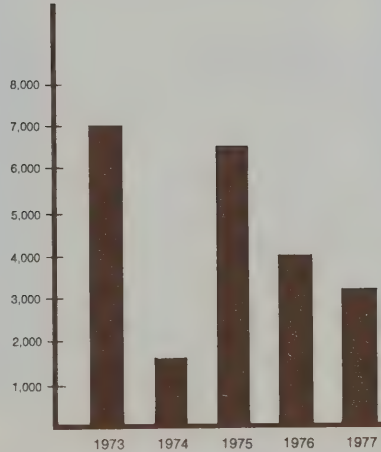
SALES PER EMPLOYEE
(\$ thousands)



CASH GENERATED
(\$ thousands)



CAPITAL EXPENDITURES*
(\$ thousands)



*includes capital value of leased equipment

Consolidated Balance Sheet as at December 31, 1977

ASSETS

	1977	1976
CURRENT ASSETS		
Accounts receivable	\$ 4,949,290	\$ 3,872,689
Income taxes recoverable		78,109
Inventory (note 3)	258,758	471,032
Prepaid expenses	164,939	156,355
	<u>5,372,987</u>	<u>4,578,185</u>
FIXED ASSETS (note 4)	<u>10,697,235</u>	<u>8,593,226</u>
OTHER ASSETS		
Deferred charges	976,648	1,031,891
Goodwill arising from acquisition of subsidiaries (note 5)	288,768	880,589
	<u>1,265,416</u>	<u>1,912,480</u>
	<u>\$17,335,638</u>	<u>\$15,083,891</u>

LIABILITIES

CURRENT LIABILITIES		
Bank indebtedness (note 6)	\$ 3,691,033	\$ 3,470,023
Accounts payable and accrued liabilities	1,711,482	2,111,210
Royalty payable	275,000	245,000
Current portion of long term debt (note 7)	173,035	386,411
	<u>5,850,550</u>	<u>6,212,644</u>
LONG TERM DEBT (note 7)	<u>7,943,940</u>	<u>6,475,642</u>
DEFERRED INCOME TAXES	<u>79,854</u>	<u>65,430</u>
MINORITY INTEREST IN SUBSIDIARY	<u>65,730</u>	<u>85,523</u>

SHAREHOLDERS' EQUITY

CAPITAL STOCK		
Authorized		
3,000 7½% Non-cumulative voting preferred shares, redeemable at par value of \$1,000 each		
6,000 Common shares without par value		
Issued		
2,250 Preferred shares	2,250,000	2,250,000
4,500 Common shares	3,002,000	3,002,000
	<u>5,252,000</u>	<u>5,252,000</u>
DEFICIT	<u>1,856,436</u>	<u>3,007,348</u>
	<u>3,395,564</u>	<u>2,244,652</u>
	<u>\$17,335,638</u>	<u>\$15,083,891</u>

Commitments (note 10)

approved by the Board

N. J. Brown
Director

W. R. Boggs
Director

Consolidated Statement of Income and Deficit

Year ended December 31, 1977

	<u>1977</u>	<u>1976</u>
REVENUE		
Information systems		
Processing	\$20,719,398	\$17,879,116
Systems design and programming	5,706,335	5,914,175
	<u>26,425,733</u>	<u>23,793,291</u>
DIRECT COSTS	15,536,989	15,520,004
	<u>10,888,744</u>	<u>8,273,287</u>
OTHER EXPENSES		
Administration	3,672,852	2,963,349
Marketing	2,824,358	2,354,858
Depreciation and amortization	1,524,401	1,298,782
Royalties	158,300	120,000
Interest		
Bank indebtedness	314,431	365,086
Long term debt	629,104	462,219
	<u>9,123,446</u>	<u>7,564,294</u>
INCOME BEFORE UNDERNOTED ITEMS	1,765,298	708,993
Income taxes (note 8)	1,044,780	554,021
	720,518	154,972
Minority interest	8,795	641
INCOME BEFORE EXTRAORDINARY ITEMS	711,723	154,331
Write-off of goodwill (note 5)	(562,811)	
Income tax reduction realized on the application of prior years' losses	1,002,000	550,000
	439,189	550,000
NET INCOME	1,150,912	704,331
DEFICIT AT BEGINNING OF YEAR	3,007,348	3,711,679
DEFICIT AT END OF YEAR	<u>\$ 1,856,436</u>	<u>\$ 3,007,348</u>

The Canada Systems Group (Est) Limited

Consolidated Statement of Changes in Financial Position
Year ended December 31, 1977

	1977	1976
WORKING CAPITAL DERIVED FROM		
Operations	<u>\$3,265,052</u>	<u>\$2,062,234</u>
WORKING CAPITAL APPLIED TO		
Purchase of fixed assets	3,070,907	2,674,010
Less long term debt incurred to finance purchases	<u>1,569,923</u>	<u>2,367,365</u>
	1,500,984	306,645
Increase in deferred charges	465,697	664,077
Acquisition of shares of subsidiary (note 2)	39,850	74,267
Reduction of long term debt	<u>101,625</u>	<u>233,267</u>
	<u>2,108,156</u>	<u>1,278,256</u>
INCREASE IN WORKING CAPITAL POSITION	1,156,896	783,978
WORKING CAPITAL DEFICIENCY AT BEGINNING OF YEAR	<u>1,634,459</u>	<u>2,418,437</u>
WORKING CAPITAL DEFICIENCY AT END OF YEAR	<u>\$ 477,563</u>	<u>\$1,634,459</u>

Auditors' Report

To the Shareholders of
The Canada Systems Group (EST) Limited

We have examined the consolidated balance sheet of The Canada Systems Group (EST) Limited as at December 31, 1977 and the consolidated statements of income and deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1977 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Canada
January 20, 1978

Thorne Riddell & Co.
Chartered Accountants

The Canada Systems Group (Est) Limited

Notes to Consolidated Financial Statements
Year ended December 31, 1977

1. Accounting Policies

(a) Basis of consolidation

The consolidated financial statements include the accounts of The Canada Systems Group (EST) Limited and its subsidiaries, Digital Methods Limited (81% owned) and L & W Data Systems Limited (wholly owned).

(b) Fixed assets

All fixed assets are stated at cost. Depreciation is provided on the straight-line basis using the following annual rates:

Building	3.33%
Auxiliary power supply	6.67 to 10%
Furniture and fixtures	10 to 20%
Equipment	16.67 to 20%

Leasehold improvements are depreciated over the terms of the leases.

(c) Inventory

Inventory is valued at the lower of cost and net realizable value.

(d) Deferred charges, which consist principally of the cost of the magnetic tapes, disks, and software, are being amortized over various periods not exceeding five years.

(e) Goodwill

Goodwill represents the excess of the cost of shares of subsidiaries over their underlying net book values at dates of acquisition, less the portion thereof allocated to tangible assets, and is amortized by the straight-line method over a period of ten years (note 5).

2. Acquisition of Shares of Subsidiary

During the year the company acquired an additional 9.5% of the outstanding shares of Digital Methods Limited, bringing the company's interest to 81%.

3. Inventory

	1977	1976
The Canada Systems Group (EST) Limited	\$217,053	\$434,691
Computer hardware (held by subsidiaries)	41,705	36,341
	<u>\$258,758</u>	<u>\$471,032</u>

4. Fixed Assets

	1977		1976	
	Cost	Accumulated depreciation	Net	Net
Land	\$ 506,758		\$ 506,758	\$ 506,758
Building	5,394,174	\$1,083,203	4,310,971	4,456,948
Auxiliary power supply	730,513	261,412	469,101	485,266
Furniture and fixtures	1,360,366	723,397	636,969	556,372
Electronic data processing equipment	5,375,264	640,621	4,734,643	2,566,396
Leasehold improvements	52,967	14,174	38,793	21,486
	<u>\$13,420,042</u>	<u>\$2,722,807</u>	<u>\$10,697,235</u>	<u>\$8,593,226</u>

5. Goodwill

	1977	1976
Balance at beginning of year	\$ 880,589	\$ 943,994
Additions	11,262	46,093
	<u>891,851</u>	<u>990,087</u>
Amortization	40,272	109,498
Write-off	562,811	
	<u>603,083</u>	<u>109,498</u>
Balance at end of year	<u>\$ 288,768</u>	<u>\$ 880,589</u>

Goodwill acquired at the date of acquisition of L & W Data Systems Limited has been written off to reflect the diminution in its value.

6. Bank Indebtedness

Included in bank indebtedness are demand loans of \$690,000 secured in part by a general assignment of accounts receivable of the subsidiary companies.

7. Long Term Debt

	1977		1976
	Current portion	Long term portion	Total
9% First mortgage, due October 21, 1996, payable \$37,260 monthly, blended principal and interest	\$ 88,098	\$4,014,945	\$4,103,043
Due to former shareholder of Digital Methods Limited, non-interest bearing, payable \$2,617 annually to April 1, 1979	2,617	2,617	5,234
Due to former shareholders of L & W Data Systems Limited, non-interest bearing	75,000		75,000
Term bank loan, bearing interest at 1% above bank prime rate, payable in five equal instalments from 1979 to 1983		2,360,000	2,360,000
Term bank loan, bearing interest at 1% above bank prime rate, payable in five equal instalments from 1980 to 1984		1,547,552	1,547,552
Finance contracts	7,320	18,826	26,146
	<u>\$173,035</u>	<u>\$7,943,940</u>	<u>\$8,116,975</u>
			<u>\$6,862,053</u>

The term bank loans are secured by chattel mortgages on certain electronic data processing equipment.

Principal due on long term debt within each of the next five years is as follows:

1978 - \$173,035 — 1979 - \$578,142 — 1980 - \$892,153 — 1981 - \$900,436 — 1982 - \$908,515

8. Income Taxes

Income taxes in 1977 of \$1,044,780 includes \$1,002,000 relating to the income of the company, and \$42,780 of current and deferred income taxes relating to the income of Digital Methods Limited. In the case of the company, no capital cost allowance was claimed in 1977 in order to maximize the amount of prior years' losses applied against income for tax purposes. Losses so applied in 1977 amounted to \$3,046,000. The tax effect of losses applied against accounting income in 1977 has been shown as an extraordinary item in the amount of \$1,002,000.

At December 31, 1977 the company and its subsidiaries have the following net amount available, the tax effect of which has not been recorded in the accounts.

Losses carried forward on a tax filing basis available to reduce future income for tax purposes until December 31:

1978	\$ 435,000
1979	744,000
1980	153,000
1981	328,000
1982	377,000
	<u>2,037,000</u>

Undepreciated capital cost for income tax purposes

10,042,007

Net book value of depreciable fixed assets

10,074,601

(32,594)

(833,915)

(866,509)

Net amount

\$ 1,170,491

9. Pension Plan

The company has a pension plan covering substantially all of its employees. Under the plan, the company is required to pay the difference between the present value of the pension benefits and the members' required contributions. Total pension costs amounted to \$362,000 in 1977 and \$419,000 in 1976.

10. Commitments

- Under the terms of a Technical Assistance Agreement with TRW Inc., dated April 29, 1971 and last amended as of December 12, 1973, the company is committed to pay, in respect of "know-how assistance", a maximum aggregate amount of \$1,775,000 during the term of the agreement which expires on December 31, 1981. Of this amount \$826,667 has been accrued in the accounts and \$551,667 paid to December 31, 1977. The balance of \$948,333 is payable in annual instalments based on certain sales as defined in the agreement, subject to a maximum payment increasing annually from \$240,000 for 1978 to \$320,000 for 1980, the balance then remaining being payable on or before June 30, 1982.
- Under terms of an agreement dated January 2, 1973, the company is committed to purchase all of the outstanding common shares of Digital Methods Limited as follows; before April 1, 1978, 6.4% and on April 1, in each of the years 1978 and 1979, 6.3%, at prices to be determined in accordance with the agreement.
- The company presently leases certain of its data processing equipment under contracts which require annual rental payments as follows:
1978 - \$3,118,139 — 1979 - \$3,052,940 — 1980 - \$979,215 — 1981 - \$7,550

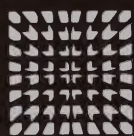
During the initial term of the leases, the company has the option to purchase some of the equipment at prices specified in the agreements. The company has the option to purchase the equipment covered by the principal leases, which expire in 1980 for \$4,103,006, or to extend such leases for further periods of up to three years, at annual rentals determined in the agreements.

11. Other Statutory Information

	1977	1976
Number of directors	7	7
Aggregate remuneration of directors as directors	Nil	Nil
Number of officers (including 2 former officers in 1977)	8	8
Aggregate remuneration of officers as officers	\$405,436	\$339,591
Number of officers who are also directors	2	2
Depreciation	\$963,190	\$389,110
Amortization of deferred charges	\$520,939	\$800,174
Amortization of goodwill	\$ 40,272	\$109,498

12. Anti-Inflation Legislation

The company is subject to the Anti-Inflation Act which provides for the restraint of profit margins, prices, dividends, and compensation. In the opinion of management the company has complied with the provisions of this Act with respect to compensation. However, as at December 31, 1977 the company had earned profits greater than those allowable under the provisions of the Anti-Inflation Act. The company intends to file a compliance plan which, in the opinion of management, will satisfy the requirements of the Anti-Inflation Board by December 31, 1978.



The Canada
Systems Group